

DOCUMENT OF INTERNATIONAL MONETARY FUND AND NOT FOR PUBLIC USE

EBS/88/51
Correction 1

CONFIDENTIAL

March 23, 1988

To: Members of the Executive Board
From: The Secretary
Subject: The Use of Limits on External Debt in Fund Arrangements

The following corrections have been made in EBS/88/51
(3/2/88):

Page 24, line 4: for "Discussion No. 623-(79/140)"
read "Decision No. 6230-(79/140)"

Page 27, line 3: for "Summing Up 83/96"
read "Buff document 83/96."

Corrected pages are attached.

Att: (2)

balance of payments projections. When limits are placed on the contracting and guaranteeing of external debt, however, it becomes necessary to estimate the consequences for disbursements within the period of debt being newly contracted. Moreover, whether debt limits are formulated on the basis of contracting or disbursement, the exclusion of certain loans or loan categories adds to the difficulty of identifying clearly the capital flows subject to the limit and relating these to other balance of payments flows.

In reports to the Executive Board, the particular specification of the debt limits should be clearly stated and their relation to the rest of the financial program explained. Both goals would be served by the presentation in staff reports of a table on capital flows oriented to a reconciliation of performance criteria in the external sector with balance of payments projections. The projected current account balance and change in gross reserves would be reconciled against a breakdown of projected capital flows including: (i) the capital flows subject to the limit on medium- and long-term debt, (ii) the capital flows subject to the limit on short-term debt (if applicable), (iii) the flows of nondebt-creating capital, and (iv) other capital flows not covered by limits on external debt. The presentation could provide whatever further breakdown of this last category would be most useful (e.g., by maturity, sector of the borrowing entity, reserve liabilities and other categories of debt explicitly excluded, etc.) and could explain, if helpful, the reasons why certain categories of debt were excluded. In the case of limits formulated on the basis of the contracting and guaranteeing of debt, the table would indicate (for the definition covered by the contracting limit) the expected disbursements from debt already contracted and expected disbursements from debt to be contracted.

Guidelines on Performance Criteria with Respect to Foreign Borrowing

The Executive Board Approves the Chairman's Summing Up
on External Debt Management Policies As Set Forth [Below]
Decision No. 6230-(79/140), August 3, 1979

The Chairman's Summing Up on External Debt
Management Policies Executive Board
Meetings 79/106 and 79/107 - July 6, 1979 and Executive
Board Meeting 79/121 - July 23, 1979

In the context of a general discussion of the issues relating to external debt management policies, the Executive Board considered the following guideline on the performance criteria with respect to foreign borrowing:

When the size and the rate of growth of external indebtedness is a relevant factor in the design of an adjustment program, a performance criterion relating to official and officially guaranteed foreign borrowing will be included in upper credit tranche arrangements. The criterion will include foreign loans with maturities of over one year, with the upper limit being determined by conditions in world capital markets; in present conditions, the upper limit will include loans with maturities in the range of 10 to 12 years. The criterion will usually be formulated in terms of loans contracted or authorized. However, in appropriate cases, it may be formulated in terms of net disbursements or net changes in the stock of external official and officially guaranteed debt. Normally, the performance criterion will also include a subceiling on foreign loans with maturities of over one year and up to five years. Flexibility will be exercised to ensure that the use of the performance criterion will not discourage capital flows of a concessional nature by excluding from the coverage of performance criteria loans defined as concessional under DAC criteria, where sufficient data are available.

Adoption of this guideline will be subject to the understanding that the staff will be guided also by the following points:

1. The above guideline will be applied with a reasonable degree of flexibility while safeguarding the principle of uniformity of treatment among members. The external debt guideline should be interpreted in the light of the general guidelines on conditionality (Decision No. 6056-(79/38), especially guideline No. 4, which states:

In helping members to devise adjustment programs,
the Fund will pay due regard to the domestic social and

1983 Review of External Indebtedness Issues--
Excerpts from Chairman's Summing Up

(Buff document 83/96 of April 14, 1983, Section 3--Guidelines on
Foreign Borrowing in Connection with Upper Credit Tranche Arrangements)

In reviewing the 1979 guidelines, the Directors made a number of comments. First, many Directors felt that normally it would be better to impose ceilings on disbursed rather than on contracted debt; nonetheless, some flexibility should continue to be used.

Second, there were divergent views on the question of including loans with maturities of from 12 to 15 years within the ceiling on loans. It was understood that if loans of 12 to 15 years' maturity were included, the concessional loans without that category should still be excluded.

Third, Directors generally encouraged the staff to include short-term debt of a maturity of less than one year in the performance criteria relating to foreign borrowing, while allowing some flexibility in light of the different institutional reporting procedures employed by members, and the statistical difficulties of recording that category of debt. In quite a number of cases, it might be necessary to formulate the limitation as a subceiling.

Fourth, normally performance criteria would exclude only concessional loans, together with restructuring and refinancing loans specifically associated with multilateral government or commercial bank loan reschedulings.

Fifth, Directors considered that, in describing adjustment programs submitted by members in connection with requests for upper credit tranche stand-by arrangements or extended arrangements, staff papers should contain a description of the proposed external borrowing limitations in the light of the prospective medium-term debt servicing profile of the member that should of course be consistent with the medium-term analysis in the staff report for the Article IV consultation.

Experience with External Debt Limits in
Fund Arrangements, 1983-1987

Experience with the use of external debt limits in Fund arrangements was last reviewed in SM/83/45 (3/8/83) which covered arrangements approved by the Executive Board over the period 1979 to 1982. ^{1/} The purpose of this annex is to review the main features of the performance criteria relating to external debt that were employed in the 117 stand-by and extended arrangements approved by the Executive Board over the period 1983 to 1987 and to describe how practices in this area differed from those of earlier years. No attempt is made in this paper to analyze, in terms of member countries' balance of payments positions, the appropriateness of the levels at which debt limits were set, rather the focus is on the design characteristics and the integration of debt limits in the financial programming exercise.

1. Frequency of use

Since the adoption of the guideline on performance criteria with respect to foreign borrowing by the Executive Board in July 1979, the use of quantitative performance criteria on external debt in Fund arrangements has become standard practice. While 93 percent of arrangements approved over the period 1979-82 contained debt limits, in more recent years the practice has been universal (Table 1).

2. Sectoral coverage of borrower

In 110 of the 117 arrangements in the sample period, the primary limit referred only to debt of, or guaranteed by, the government or the public sector (Table 2). Of the 72 cases where entities outside the Central Government were covered, certain public sector entities were excluded in roughly half of the cases, while the entire public sector was covered in the rest. In seven arrangements with four countries (Brazil, Korea, Philippines, and Portugal) that were viewed as having the capacity to monitor the debt of all sectors, coverage extended to include private sector borrowing (including loans without government guarantee).

3. Form of limitation

In 90 of the arrangements reviewed, the primary debt limit related to the contracting or guaranteeing of external debt. In 27 arrangements, limits were placed on the disbursement of debt, mainly in the form of a limit on the level or increase in the stock of debt

^{1/} A brief review of recent experience with performance criteria on external debt was contained in Program Design and Performance Criteria (EBS/86/211, Sup. 1, 9/11/86). Earlier experience with external debt limits in upper credit tranche arrangements, over the period 1973 through January 1979, was reviewed in SM/79/125 (5/11/79). This paper also contained references to papers reviewing developments prior to 1973.